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IN THE

Supreme Court of the United States

OCTOBER TERM, 1941.

No. 204

NETTIE MEYER, ANNA JACOBSON, JACOB MEYERHOFF, JOSEPH MEYERHOFF, JULIUS MEYERHOFF, RAY MANN AND JOHN J. PANKIN,

Petitioners,

vs.

KENMORE-GRANVILLE HOTEL COMPANY, SAMUEL J. T. STRAUS, MELVIN L. STRAUS, M. A. ROSENTHAL ET AL.,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE APPELLATE COURT OF ILLINOIS, FIRST DISTRICT, AND BRIEF IN SUPPORT THEREOF.

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PETITION FOR WRIT OF CERTIORARI TO THE APPELLATE COURT OF ILLINOIS, FIRST DISTRICT, AND BRIEF IN SUPPORT THEREOF.

To the Honorable the Chief Justice and Associate Justices of the United States:

Petitioners, Nettie Meyer, Anna Jacobson, Jacob Meyerhoff, Joseph Meyerhoff, Julius Meyerhoff, Ray Mann and John J. Pankin, Pray the issuance of a Writ of Certiorari to review the judgment of the Appellate Court of Illinois for the First District whose judgment was made final by the denial of leave to appeal by the Supreme Court of Illinois on April 10, 1941.

Statement of the Matter Involved.

Petitioners are a group of investors who purchased Gold Bonds from S. W. Straus & Co. (hereafter referred to as "Straus") secured by two trust deeds, one on the Sovereign Hotel, and the other on the Annex, for $1,000,000 each. Petitioners' action for accounting against the two trustees, who were in possession of the mortgaged premises after default for several years, and against the Protective Committees who betrayed their trust duties, was held to be barred by a defense of *res adjudicata* based on proceedings in the District Court under section 77B.

Material facts "Straus" floated two bond issues for $1,000,000 each, one on the Sovereign Hotel, in 1919, and another on the Annex, in 1922. The officers of "Straus", Samuel J. T. Straus, President, and Melvin L. Straus, Vice-President, were the trustees of the "Sovereign" and "Annex" respectively. The Annex Bond Issue contained a personal guarantee of the principal shareholder (R. 38). Default was made in the first years' taxes after the construction of the Annex. Both properties were sold for the non-payment of the 1923 taxes (R. 38). Defaults in principal and interest followed and the two trustees entered into possession on May 8, 1925 and remained in possession until 1934 (R. 39). The petitioners were not informed of these facts until January 29, 1931 when they were urged to deposit their bonds with Protective Committees headed by Straus officials (R. 35). The two trustees deposited the net income with "Straus", which income was used to reimburse it for principal and interest advanced to the unaware bondholders. Many of the deposits were made as late as three months after maturity (R. 40, 41). During that period "Straus" obtained title to the mortgaged premises via a junior foreclosure, subject to the continuing lien of the bond issue. It obtained a

Master's Certificate on December 19, 1929 in the name of Sidney H. Kahn, one of its vice-presidents, who headed one of the Protective Committees. The trustee, Samuel J. T. Straus, headed the other Protective Committee (R. 35). After thus acquiring the properties, "Straus" solicited the deposit of the bonds with its Committees. These Committees adopted a Plan of Reorganization which called for the formation of a corporation to acquire the properties at the foreclosure sale, to exchange the bonds for common stock, giving 10% to "Straus" and 90% to the investors under a Voting Trust, which vested control of the property in "Straus". This plan, which was prevented by petitioners' suit, was carried out in the Federal Court under Section 77B with some modifications. As a result of the reorganization, petitioners' bonds were exchanged for stock whose value is eight cents on the dollar (R. 27, 28). The action of the petitioners against the trustees and the committee members for accounting, malfeasance and misfeasance was barred by the defense of *res adjudicata* based upon the 77B proceedings, and petitioners will lose 92% of their investment.

History of the Litigation Which Barred This Proceeding Nettie Meyer, one of the petitioners, was the only plaintiff in the suit commenced by her on February 8, 1935 seeking an accounting from the trustees, and the prevention of the fraudulent reorganization plan by the Straus Committees. She served notice on March 12, 1935 that she would appear in court on March 13, 1935 and ask for the appointment of a receiver and the restraining order. On that day the respondents filed a consent to the approval of an involuntary petition for corporate reorganization under Section 77B,* obtained the approval of the petition and restrained the proceed-

* This consent was given by the corporation which Straus organized and which acquired title from Kahn in 1932 (R. 37) but which never functioned as the property was either in possession of the Trustees or in possession of a tax receiver.

ings in the State Court (R. 48). Nettie Meyer filed her petition in 77B proceedings seeking to set aside the orders for lack of good faith and jurisdiction,** and the respondents moved to strike her petition (R. 48, 49). The District Court rendered on opinion on March 20, 1937 to the effect that the restraining order will not prevent the action for accounting, malfeasance and misfeasance provided it will not interfere with the 77B proceeding (R. 46). It denied the motion to vacate the orders but refused to strike the petition and ordered that due notice be given to counsel for Nettie Meyer on all further proceedings. Nettie Meyer appealed from this under 24a, and on May 21, 1935 the Seventh Circuit dismissed the appeal on jurisdictional grounds (77 Fed. (2d) 1004). The other petitioners, who were later joined as parties plaintiffs to the suit of Nettie Meyer, filed objections and suggested modifications to the Plan. On February 27, 1935 the District Court sustained some of the objections and approved the Plan as modified, including that part of the Plan which gave "Straus" a 10% interest in the reorganized property (R. 50, 51). Leave to appeal was denied by the Seventh Circuit on June 25, 1935, and the appeal taken under 24a was dismissed on jurisdictional grounds 78 Fed. (2d) (1118). This court allowed certiorari on the dismissal of the two appeals (296 U. S. 565) and finally decided that the appeals were properly dismissed on jurisdictional grounds (*Meyer* v. *Kenmore-Granville Hotel Co.*, 297 U. S. 160). On November 23, 1936 the District Court entered an order, without notice to petitioners' counsel, dismissing the petition of Nettie Meyer and ordering a release of the two trust deeds. Petitioners filed a petition on December 4, 1936 seeking to vacate the order (R. 52). This matter was referred to referee upon the answer to the petition. On February 25, 1937 the District Court approved the report of the referee and dismissed the petition. Within the term time it entered

** The attack was based on the facts stated in the above note.

a final decree discharging the Debtor. Petitioners applied for leave to appeal under 24b which was denied (90 Fed. (2d) 151). They prosecuted an appeal under 24a from both orders, which appeal was dismissed on the ground that petitioners were dismissed out as interveners and had no right to appeal (92 Fed. (2d) 778). This court denied certiorari on January 17, 1938 (302 U. S. 767). The respondents urged on the appeal in the Seventh Circuit (R. 45) that the adjudication in the 77B proceeding could not be pleaded in bar of petitioners' action in the State Court for accounting and for malfeasance and misfeasance (R. 45, 47).

The Proceedings For the Accounting. After the denial of certiorari by this court making final the order discharging the Debtor and completing the reorganization, petitioners filed an Amendment to their Complaint (R. 11-13) setting forth the proceedings in the Federal Court which culminated in the approval of the Reorganization Plan and eliminated that part from the Complaint limiting the action to the following (R. 12):

> 1. The liability of the two trustees for failure to disburse the income which they received as trustees in possession during the six-year period from 1925 to 1931 and whose duty it was to distribute direct to the bondholders under the terms of the Trust Indenture and which they diverted to the benefit of their house wherein they were vitally interested.
>
> 2. The liability of the two trustees for damage caused as a result of the concealment of the facts that they were in possession because of defaults from 1925 to 1931 by reason whereof the bondholders were prevented from seeking a foreclosure prior to the collapse of real estate values which would have yielded 100% on their investment and which later brought them only 8 cents on the dollar.
>
> 3. Injury resulting to the bondholders as a result of the concealment of the existing defaults during the

six-year period from May 8, 1925 to January 21, 1931, whereby they were prevented from enforcing their remedy on the personal guaranty of the principal stockholder.

4. A general accounting against the two Trustees for all funds collected and disbursed by them from the operations of the mortgaged premises from 1925 to 1934 during their tenure as Trustees in possession.

5. Loss resulting from the breach of duty of the members of the Protective Committees who served the interest of "Straus" instead of the interest of the petitioners who entrusted the bonds with them for protection.

The respondents filed their respective answers and a hearing was commenced before the chancellor on these pleadings. On the first day of the hearing the respondents obtained leave to file an Amendment to their Answer setting forth the defense of *res adjudicata* based on the Federal Court proceedings (R. 22, 23). Petitioners filed their reply urging (1) the estoppel of the respondents to interpose the plea and (2) that the 77B proceedings could under no circumstances be pleaded in bar to this action (R. 23-25). The chancellor heard the case on its merits and made no ruling on this defense. He dismissed the case for "want of equity" (R. 25). The Appellate Court affirmed his decree on the ground that the defense of *res adjudicata* was a complete bar to the action. The decision of the Appellate Court was rendered January 20, 1941 (R. 59). A petition for rehearing was filed February 5, 1941 (R. 59) which raised the point that the Appellate Court deprived the petitioners of their property without due process of law in violation of the Fifth and Fourteenth Amendments to the Federal Constitution in sustaining the defense of *res adjudicata* (see appendix). Rehearing was denied on February 5, 1941 (R. 59). The Supreme Court of Illinois denied leave to appeal on the 10th day of April, 1941.

Questions Presented.

1. Whether petitioners were deprived of due process of law as guaranteed by the Fifth and Fourteenth Amendments to the Federal Constitution, when the Appellate Court sustained the defense of *res adjudicata* based on the 77B proceeding, notwithstanding the position of the respondents on the appeal in the Seventh Circuit that such proceedings could not be pleaded in bar to the action for the accounting.

2. Whether the petitioners were deprived of due process of law by the Appellate Court of Illinois when it sustained the defense of *res adjudicata* based on the reorganization proceeding, in which proceeding the federal jurisdiction was confined to the *res* and not to the action in *personam* against the trustees and the Committees for accounting, malfeasance and misfeasance.

3. Whether a confirmation of a reorganization plan under Section 77B may be pleaded in bar to an action for accounting and fraud against trustees and protective committees.

4. Whether the federal question was properly presented below and whether the decision below may be sustained on a non-federal question.

Reasons for the Allowance of the Writ.

1. The decision of the Appellate Court of Illinois that an order confirming a reorganization under 77B may be pleaded in bar to an action for fraud, malfeasance, misfeasance and accounting against trustees and committees is contrary to the decisions of this court and involves matters of great importance relating to federal procedure.

2. The judgment of the State Court is challenged for due process and this court will exercise its discretionary

power to examine the course of the proceedings to ascertain whether petitioners were accorded due process.

3. The question whether adjudications in 77B, or Chapter X proceedings may be pleaded in bar to an action for accounting against trustees and committees deserves the exercise of the discretionary power of this court to issue the Writ.

PRAYER FOR RELIEF.

WHEREFORE, the above petitioners pray the allowance of a Writ of Certiorari to the Appellate Court of Illinois, First District, to the end that the decision of the Appellate Court rendered January 20, 1941 and made final by denial of leave to appeal on April 10, 1941 may be decided by this court and that the judgment be reversed.

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